

Construction contracts for the improvement of real estate consisting of engineering, installation, and maintenance of voice, data, video, security, and all telecommunication systems do not constitute engaging in a business of selling tangible personal property at retail within the meaning of the Retailers' Occupation Tax Act if they are sold at one specified contract price. See 35 ILCS 120/1 and 86 Ill. Adm. Code 130.1940(c)(3). (This is a PLR.)

December 21, 2005

Dear Xxxxx:

This letter is in response to your letter dated December 21, 2004, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

Review of your request disclosed that all the information described in paragraphs 1 through 8 of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to ABC for the issue or issues presented in this ruling, and is subject to the provisions of subsection (e) of Section 1200.110 governing expiration of Private Letter Rulings. Issuance of this ruling is conditioned upon the understanding that neither ABC nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request. In your letter you have stated and made inquiry as follows:

An Illinois Dept. of Revenue auditor completed an audit of our company, ABC, in November 2004. The auditor determined that the manner in which we apply sales tax to all of our equipment sales is appropriate, but warned us that another auditor may take an alternative view. Therefore, we are seeking a written Private Letter Ruling to direct our company in the proper way to apply Sales or Use tax to our sales from here forward.

Company background

ABC's one location is located in Illinois. We are a sub-chapter-S corporation and have been selling and installing video surveillance camera systems and other low voltage equipment for 26 years. Our clients are typically in the CITY area, but may also be in STATES, with whom we are also registered to collect sales tax. We have a file of tax-exemption letters from many of our clients including hospitals, schools, and

municipalities, but about half of our clients are not exempt – office buildings, banks, manufacturing facilities, etc.

Typical transaction

Our five salespeople call upon prospective clients at their offices. We determine the best equipment to solve the clients' problems with theft, vandalism, quality control, crowd control, etc. The price of the proposed equipment is quoted in at least three categories: cost of equipment, sales tax on equipment, and cost to install. In bid situations it is not uncommon to quote a job in a lump sum, but then every invoice is clearly divided into equipment, sales tax, and labor.

The Equipment

The typical system includes cameras, VCRs or digital storage devices, lenses, monitors, and other accessories. Our technicians begin an installation by running cable between the designated camera sites and the head-end equipment (the brains of the system including perhaps a VCR, computer storage, controllers, and monitors). Technicians also mount metal brackets to walls to which cameras or pan-and-tilts will be attached later. The head-end equipment may be set upon shelves, desks, or in a workstation.

The question is: Do we lump ourselves in with construction companies and build in a use-tax on all of the equipment; or do we charge the higher sales tax on all of the equipment? Or do we somehow divide up the tax between the two? Charging ourselves Use tax on a small part of every job becomes more difficult since about half of our clients are tax exempt.

1) Statement of Facts:

About 50% of each invoice is attributable to equipment. Typically, about 10% -20% of that 50% is for hardware and cable. Hardware is defined as the nuts and bolts, and metal brackets to hold the cameras or other equipment to be attached to the walls and/or ceilings. The percentage range depends upon the length and complexity of the cable runs and whether or not local codes require conduit.

80%-90% of the equipment for camera installations is high value electronics (cameras, computers, monitors) which we do not think should be considered part of the real estate because we can and do swap them out when they need repair or when the client remodels or up-grades to new equipment.

We also install access control systems, burglar alarms, and, infrequently, intercom systems. This type of installation uses a higher percentage of labor. . . about 70% labor. The remaining 30% of the invoice represents equipment; of that between 10%-20% is attributable to the low-cost hardware and cable while the majority of the cost is for the electronics -- door access readers, computers, digital alarm panels, amplifiers. While readers and panels may be attached to the wall, we frequently swap them out for repairs or up-grades.

2) Contracts; licenses

Enclosed please find our Department of Professional Regulations license, a sample invoice, a typical proposal, and a blank contract.

3) Tax period at issue - all future

4) Statement - No written ruling has ever been received or formally requested.

5) Supporting view - In addition to the auditor to perform the November, 2004 audit, an auditor performed a Sales Tax audit in about 1989 or 1990. He also was of

the opinion that the way we charged sales tax on all equipment, hardware and cable was the appropriate way, rather than considering all or part of our systems permanent real estate fixtures and paying use tax. Although a written determination was verbally requested from Springfield, none was given.

6) Contrary View - None known.

7) 'none'

Summary

Since the majority of the equipment used in our camera, alarm, and access control systems is movable, we believe that Sales Tax should be charged to the client on all of the equipment, including the hardware, brackets, cable, and conduit. Applying sales tax to all equipment is more appropriate, more efficient, easier to implement and to understand for us and the end-user, and provides more revenue for the state.

Please issue a written determination letter, stating that Use tax does not apply (except when removing an item from inventory for our own, in-office use) and that Sales Tax is the appropriate tax for all of our transactions (except tax-exempt and for resale, etc.)

If I can further clarify any issue, please call my office and leave a message with a direct phone number and an appropriate time for me to return your call. Thank you for your timely consideration of this matter. I look forward to receiving your Private Letter Ruling.

DEPARTMENT'S RESPONSE:

Based on the information provided, we believe that ABC contracts to provide an installed security system for its customers. This means that, as opposed to a business model in which the retailer sells security systems, and then, in some instances, enters into an additional agreement to install the systems, ABC's standard procedure is to both sell and install the security systems. When ABC agrees to sell and install a security system so as to make it a permanent part of a building, ABC is acting as a construction contractor. A construction contractor is deemed to be the end user of the materials which he takes off the market and incorporates into real estate. The construction contractor will incur Use Tax on his cost price of the tangible personal property incorporated into real estate. When a construction contractor subsequently sells and installs property in a fashion that makes the property a real estate improvement, there is no sales tax due because sales tax does not apply to sales of real estate improvements. The contractor simply discharges the tax liability "up front" by paying tax at the time he buys the materials. See 86 Ill. Adm. Code 130.1940.

When ABC sells and installs a security system, the customer incurs no Use Tax and, as a construction contractor, ABC has no authority to collect Use Tax from the customer. Many construction contractors pass on the amount of their Use Tax liabilities to customers in the form of higher prices or by including provisions in their contracts that require customers to "reimburse" the construction contractor for his or her tax liability. Please note that this reimbursement cannot be billed to a customer as "sales tax," but can be listed on a bill as a reimbursement of tax. The choice of whether a construction contractor requires a tax reimbursement from the customer or merely raises his or her price is a business decision on the construction contractor's part.

In the specific case of installers of security systems, Section 1 of the Retailers' Occupation Tax, in an attempt to ease the burden of administration, provides specifically that "[c]onstruction contracts for the improvement of real estate consisting of engineering, installation, and maintenance of voice, data, video, security, and all telecommunication systems do not constitute engaging in a business of selling tangible personal property at retail within the meaning of this Act if they are sold at

one specified contract price.” See 35 ILCS 120/1. Subsection (c)(3) of Section 130.1940 of the Department’s administrative rules elaborate on this further by stating “[t]his provision applies to all of the items . . . even if they are not incorporated into real estate.” See 86 Ill. Adm. Code 130.1940(c)(3).

As a result of the statutory and regulatory language, installers of security systems are authorized to pay Use Tax to their providers on all equipment and supplies they purchase related to the security systems they sell and install, even if some of those supplies are not technically incorporated into real estate, such as the cameras, computers and monitors described in your letter. This provision applies if the sale and installation of the security systems are packaged for one specified contract price, as ABC currently does.

Subsection (d) of Section 130.2075 addresses sales to construction contractors of materials to be used in a contract with a customer who has a sales tax exemption number issued by the Department. The regulation states that the sale of materials to contractors acting for tax-exempt organizations is exempt from Retailers' Occupation Tax and Use Tax. A supplier claiming exemption in this situation must follow the procedures outlined in Section 130.2075(d)(4). In order to take advantage of its customer's exempt status, when purchasing the equipment ABC must provide its supplier with the active exemption number issued by the Department to the organization for which ABC is acting.

The factual representations upon which this ruling is based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the factual representations recited in this ruling are correct and complete. This Private Letter Ruling is revoked and will cease to bind the Department 10 years after the date of this letter under the provisions of 2 Ill. Adm. Code 1200.110(e) or earlier if there is a pertinent change in statutory law, case law, rules, or the factual representations recited in this ruling.

I hope this information is helpful. If you have further questions concerning this Private Letter ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.tax.illinois.gov or contact the Department’s Taxpayer Information Division at (217) 782-3336.

Sincerely,

Samuel J. Moore
Associate Counsel

SJM:msk